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SUBJECT: PAKISTAN'S APPEAL FOR WHEAT THROUGH THE GSM 102 PROGRAM

¶1. (SBU) Summary. The Government of Pakistan (GOP) faces a wheat shortage of 1.75 million tons, valued at approximately USD 450 million. Post recommends approval of a USD 450 million U.S. Department of Agriculture (USDA) GSM-102 credit guarantee program for Pakistan in FY 2009 to support sales of U.S. wheat, address the needs of the poorest people of Pakistan, and enhance food security throughout the region, including in Afghanistan which receives 45 percent of its wheat from Pakistan. Although Pakistan defaulted on the GSM-102 program between 1998 and 2002, payment of the debt has subsequently been rescheduled through 2024. Post believes this program, if timed to coincide with the announcement of the IMF program, could provide a vote of confidence for the democratically elected government of Pakistan and serve as a symbol of U.S. support for Pakistan's economic difficulties. End Summary.

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WHEAT DEFICIT GOING INTO THE WINTER  
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¶2. (SBU) Wheat stocks currently held by the GOP (3 million tons) are only sufficient to meet domestic consumption needs through January 2009, as the government releases stocks to the provinces at the rate of about 1 million tons of wheat per month. Pakistan will not harvest its next wheat crop until April/May 2009; therefore, it needs additional imports of 1.75 million tons (at an estimated cost of USD 450 million) to avoid shortages in February and March. Pakistan's total wheat import needs for the 2008/2009 marketing year are estimated at 3.5 million tons. To date, the GOP has secured imports of 1.7 million tons of red wheat and 50,000 tons of white wheat. To meet the country's consumption needs until it harvests the next crop, the government must purchase an additional 750,000 tons of red wheat and 1 million tons of white wheat. Pakistan typically imports wheat at a ratio of 70 percent red wheat and 30 percent white wheat.

¶3. (SBU) The April 2009 crop is expected to be lower than planned due to water and fertilizer shortages. Irrigation for the current crops has fallen due to a combination of low rainfall and a water dispute with India, which has resulted in a 34 percent drop in water levels. Fertilizers, both Diammonium Phosphates (DAP) and urea, are in short supply as producers are said to be hoarding or smuggling stores. Winter just began in Pakistan (typically November through February) and a food shortage will aggravate Pakistan's many problems, especially if the economy continues to contract and energy

blackouts continue in food insecure regions.

14. (SBU) Recently, the World Food Program (WFP) identified Pakistan as one of 40 countries in the world at risk for food insecurity. The WFP raised its estimate of at-risk individuals from 60 to 77 million, or 48 percent of Pakistan's population. Over 100 million Pakistanis live on less than two dollars per day, including 27 million living on less than one dollar per day. The cost of wheat has risen 68 percent in the last twelve months, which has placed this basic commodity out of reach for many average citizens. However, current supplies are insufficient to meet demand through the winter. This will lead to further price increases if additional wheat is not available before the next harvest.

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IMPACT ON AFGHANISTAN  
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15. (SBU) While Post defers to our colleagues in Kabul, it seems as if GSM credits for Pakistan would also help alleviate potential wheat shortages in Afghanistan. Like Pakistan, the World Food Program has also labeled Afghanistan as one of 40 food insecure countries. A severe drought in Afghanistan has led to a 60 percent decline in this year's wheat crop. Historically, some of the shortfall in Afghanistan's wheat production is filled through legitimate imports from Pakistan. But due to an artificially low wheat price in Pakistan, traders are now regularly smuggling Pakistani wheat into Afghanistan. Pakistan supplies about 45 percent of Afghanistan's wheat needs.

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16. (SBU) This year, the Pakistani government raised by 48 percent the government purchase price of wheat. (The international community had strongly urged an increase in the artificially low government purchase price of wheat.) The GOP plans another 52 percent increase in the government purchase price in April 2009. An increase in domestic wheat prices in Pakistan will eventually encourage more domestic wheat production and less hoarding. However, as prices in Afghanistan and Pakistan reach parity, it will become less attractive for Pakistanis to either sell or smuggle wheat to Pakistan.

17. (SBU) The combination of rising prices and the shortfall in wheat imports should cause wheat prices in Pakistan to rise sharply. If the GSM credits can encourage imports, local supplies should be greater, price increases should be less, and more Pakistani wheat should be available in Afghanistan.

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GOP REQUEST FOR GSM-102: NEED FOR WHEAT  
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18. (SBU) The GOP has approached Post requesting an expansion of the USDA GSM-102 credit guarantee program to cover Pakistan's near-term wheat import needs. The GSM-102 program helps ensure that credit is available to finance commercial exports of U.S. agricultural products by providing competitive credit terms to buyers. By reducing the financial risk to U.S. lenders, the GSM-102 program encourages exports to countries, such as Pakistan, where financing (and therefore sales) might not be available without the program.

19. (SBU) The Trading Corporation of Pakistan has approved five Pakistani banks to finance wheat purchased by the GOP. These Pakistani banks would borrow money from U.S. banks to purchase the U.S. wheat. The loans offer favorable interest rates because the USDA (i.e. the USG) guarantees payment, under the GSM-102, to the U.S. banks. In August 2008, the GOP provided the USDA with a Credit Guarantee Assurance, or sovereign guarantee, whereby the GOP guarantees all GSM-102 wheat purchases by the approved Pakistani banks in any amount. Under the current GSM-102 program, the total exposure available for Pakistan for FY 2009 is USD 48.01 million.

110. (SBU) Per the program rules, USDA will need to waive the total exposure guideline if Pakistan is to purchase its wheat import requirements under the GSM-102 credit guarantee program for any

amount above the USD 48.01 million maximum cap. On September 20, Ministry of Food, Agriculture and Livestock (MINFAL) Secretary Muhammad Zia-ur-Rehman wrote the Ambassador asking for a USD 400 million expansion of its existing request for a USD 100 million GSM 102 facility for the procurement of wheat. Thus, the total GOP request for GSM-102 is USD 500 million, which roughly represents the cost of importing 1.75 million tons of wheat at the time the request was made. Post notes that the international price of wheat has since decreased. Therefore, Post estimates that USD 450 million would cover Pakistan's short term import costs.

¶11. (SBU) Contacts in the Trading Corporation of Pakistan and MINFAL inform Post that if sufficient credit guarantees are made available under the GSM-102 program, the GOP will probably purchase most of its near-term wheat import requirements from the U.S. Timing is important, however, as wheat shipments from the U.S. to Pakistan take a minimum of 45 days. Pakistan has not purchased wheat since August 7 and even then the transaction amounted to only 210,000 tons of red wheat. In short, Pakistan urgently needs the additional wheat imports to avoid food shortages.

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HELPING WITH FOOD INSECURITY  
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¶12. (SBU) During Prime Minister Yousaf Raza Gilani's visit to Washington in July 2008, President Bush committed to providing USD 115.5 million in food security assistance to Pakistan, including USD 24 million for the Food for Progress plan, USD 10 million for the McGovern-Dole program, and USD 8.5 million in Economic Support

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Funding (ESF) for USAID's agricultural program. These programs are underway and provide food in some of Pakistan's most remote areas. However, these programs support on-going school feeding programs and supplemental food aid for WFP operations in Pakistan. None of these programs can provide short term relief for the wheat shortfalls this winter.

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FINANCIAL SITUATION  
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¶13. (SBU) Pakistan is working closely with the International Monetary Fund (IMF) to reach a stabilization program and to increase Pakistan's foreign exchange reserves. The announcement of a USDA GSM-102 program concurrent with Pakistan's adoption of an IMF package would enhance Pakistan's ability to meet its international commitments and help restore economic stability in the region. It would also provide a vote of confidence in the GOP and the IMF plan.

¶14. (SBU) Pakistan defaulted on debt accrued under the GSM-102 program between 1998 and 2002. Economic mismanagement coupled with U.S. and international sanctions imposed after the completion of nuclear tests in 1998 made it difficult for Pakistan to meet its obligations. GOP debt under the GSM-102 program totals USD 284 million; however, payment of this debt subsequently has been rescheduled through 2024. Pakistan has not utilized the GSM 102 program since FY 1999 due to the combination of relatively good wheat crops, availability of lower-priced wheat from Black Sea sources, better fiscal position of the government, and until recently, the availability of cheap international credit.

¶15. (SBU) Comment: The economic situation in Pakistan is tenuous, and the GSM-102 program offers an opportunity to provide the poorest people of Pakistan, and by extension Afghanistan, relief from potential wheat shortages during the critical winter months. The program would contribute to enhancing food security and allow U.S. producers to make a significant wheat sale on commercial terms. Coordinated timing of this program would allow the USG to demonstrate its support to the GOP and IMF plan or, alternatively, could be announced at the upcoming Friends of Democratic Pakistan meetings. Post recommends approving a GSM-102 program commensurate with Pakistan's needs to ensure that the GOP has the ability to purchase additional imports of 1.75 million tons of wheat at an

estimated cost of USD 450 million. End Comment.

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